STATEMENT OF
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BEFORE THE
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Thank you Mr. Chairman and Members of the Committee. I am pleased to be able to discuss domestic aviation issues with you today.

A top priority of economic policy set out in our implementing statutes is the maintenance of competition in U.S. domestic airline service. We view this priority as second only to the maintenance of safety. Just as safety was not deregulated in 1978, neither was the Department's responsibility to do what it can to maintain a competitive domestic airline industry, keeping in mind the statute's directive that we place "maximum reliance on competitive market forces".

Seven years ago the Department took a thorough look at competition in the multi-volume study known as the "Secretary's Task Force on Competition in the U.S. Domestic Airline Industry". In that study the Department concluded that deregulation had been an overall success. The creation of competing nationwide hub and spoke networks during the 1980's had led to better, more competitive service for the vast majority of consumers, and average fares in the U.S., adjusted for inflation, were down substantially. That study also noted that not all travelers and markets have enjoyed the same level of benefits--that there were "pockets of problems". In particular, we found that fares at network hubs dominated by a single carrier were high, especially in shorter haul markets.

Our views on the overall success of deregulation have not changed. On average, inflation adjusted fares have continued a long term trend downward through 1996. Since 1981, the first year when air carriers had actual pricing freedom, the average real fare in the U.S. has fallen 37.2 percent. Well-timed, frequent service for most cities made possible by the

move to hub and spoke systems continues. As an overall matter, we know competition in domestic aviation continues to work to the benefit of the vast majority of consumers. And judging by its recent reports, we believe the General Accounting Office would agree with that assessment.

For several years we were encouraged that the problem of high fares in certain hub markets was being slowly solved by new competition in the marketplace. In 1993 a Department study noted the major impact that a low-fare point-to-point carrier, Southwest Airlines, was having on short haul fares in dense markets, many involving concentrated hubs where one major airline interconnected traffic and had the overwhelming share of enplanements. And since the beginning of 1993 there had been a steady stream of new entrant airlines, many of which were using the low-fare approach of Southwest. In April of 1996, the Department issued a study entitled "The Low-Cost Airline Service Revolution" that documented how Southwest and this newer group of airlines were saving consumers an estimated $6.3 billion annually in airline fares, $2.6 billion of which was being saved in concentrated hub markets. That study noted that virtually all of the domestic traffic growth in recent years was due to the competitive impact of these low fare carriers. The major network airlines appeared to be able to live side-by-side with the newer competitors and the majors were becoming more efficient as a result.

In spite of this generally positive picture, however, there continued to be competitive problems in specific markets. Our April 1996 study pointed out that fare premiums at some eastern and midwestern hub cities had increased dramatically since our 1990 study. Various traditional barriers to entry such as limited gates or slots may be part of the explanation for high fares in some hub markets. But we are becoming increasingly concerned that another important barrier may be overly aggressive exclusionary behavior of major airlines toward new entrants that attempt to compete at these dominated hubs.

For several years the Department has been informally addressing allegations by smaller carriers that major network airlines are using anticompetitive tactics in an attempt to thwart new entry. But recently the Department has had an increasing number of visits from the smaller carriers, and they are becoming more vocal in their complaints. Since the tragic Valujet accident in Florida last May, the expansion of competition from low-fare carriers has slowed substantially. New entry has almost

completely stopped. We have received no new low-fare applications this calendar year and we have licensed only one new low-fare competitor since the accident. We know that several companies that were close to applying for authority found that capital was drying up and the time was not right to start a new low-fare airline. The capital markets and the American traveling public were clearly feeling an unease about these companies. It has been alleged that since the government was focusing on the safety aspects of low-fare carriers and the American public was nervous, major carriers determined it was a good opportunity to step up their activity against these smaller companies.

The kinds of practices the smaller carriers are complaining about typically include the larger airlines temporarily matching, or in some cases allegedly undercutting, the much lower fares that these low-cost carriers can provide and offering an increased number of seats in the local hub markets at these low fares in an alleged attempt to eliminate the new entrants from the city-pair market. Also, there are complaints about extra capacity being added on their routes, and bracketing with extra flights the flight times of the new carriers. There are concerns that the larger carriers are re-entering markets they had abandoned as unprofitable, merely to overwhelm the smaller companies. The older carriers are also accused of selectively using hub dominance advantages, frequent flyer programs, computer reservation systems, travel agent relationships and even dirty tricks to prevent the spread of low fare competition.

While the Department has not yet come to any definitive conclusions about the scope and extent of these alleged acts, nonetheless, all of these activities, together with other barriers to entry such as airport access issues, have raised a concern at DOT about the need for appropriate action.

With regard to allegations of anticompetitive activity, both the Department of Transportation and the Antitrust Division at the Department of Justice are actively studying cases where predatory practices have been alleged by smaller airlines. Predation under the antitrust laws can be very difficult to prove based on court precedents, particularly in the manufacturing sector. Section 41712 of title 49 U.S.C. gives the Secretary of Transportation authority to act on complaints of unfair methods of competition and represents broader authority than the antitrust laws to prohibit such unfair acts. The Secretary has the power to act even if the practice does not violate the antitrust laws, but is similar to an antitrust violation. At the

same time, we recognize that honest competition and the benefits that it affords consumers must be preserved.

The operating structure of the airline industry makes it difficult to deal with anticompetitive issues in traditional ways. The Department is studying how section 41712 can be applied to complex airline industry commercial practices.

Under section 41712 the Secretary may determine that a practice is an unfair method of competition either in an enforcement case against one airline or in a rulemaking that would have a prospective impact on all airlines.

We will continue to work with the Department of Justice in reviewing anticompetitive activity and action will be taken where appropriate under either authority.

The Department also believes that consumers are entitled to be aware of the effects of competition on fares. Therefore, the Department is considering the dissemination of information on actual fares consumers pay in the various city-pair markets around the nation. The Department's consumer reports covering on-time performance, lost baggage and consumer complaints have had a positive effect in helping to modify airline behavior.

The Department is not alone in its concerns. Actions by private groups are also being taken to help to bring about better fares in markets where low fare competition has not developed. I understand that one company is organizing corporations to help reduce business fares in markets by guaranteeing support for low fare carriers in selected high fare markets.

Cities have also become more active in trying to develop better service and lower fares for their residents. As an example, a roundtable discussion was held in Chattanooga, Tennessee, which Senator Bill Frist of this Committee helped to organize. The meeting addressed innovative actions that could be taken to help bring a competitive market for air services to mid-sized communities. Ideas were developed such as consumer education at the local level as to the benefits of supporting new-entrant carriers, and the offering of financial incentives by local governments in concert with the

private sector to carriers to provide new service by guaranteeing a particular level of revenue or providing direct promotional support.

Specific operational barriers to entry have been addressed by the GAO. In its recent report to this committee entitled "Airline Deregulation--Barriers to Entry Continue to Limit Competition in Several Key Domestic Markets" the GAO argued that takeoff and landing slots at Chicago's O'Hare, New York's JFK and LaGuardia and Washington's National airports and the lack of gate availability at some other airports generally located in the northeast quadrant of the country have contributed to the high hub fares. The GAO report had several suggestions and recommendations to alleviate the competitive problems created by these operating barriers, including a suggestion that Congress permit exemptions to the perimeter rule at National Airport if proposed service would substantially increase competition.

The primary GAO recommendation regarding the four slot controlled airports was for the Secretary of Transportation to create a pool of available slots by periodically withdrawing some slots that were grandfathered to the major incumbents when the buy-sell rule was created and holding a lottery to distribute them in a fashion that increases competition. The Department in its formal response to the GAO report indicated that it would consider that suggestion. The Department also took note of a GAO suggestion that Congress may wish to revise the legislative standard governing the Secretary's granting of additional slots to accommodate new entrants, making competition a key criterion. The Department stated that even without a change in legislation, it intended to be more receptive to considering competition as a factor in granting slot exemptions to new entrants under the "exceptional circumstances" criterion in the law.

With regard to gate availability, GAO recommended that the Secretary of Transportation direct the FAA Administrator to make an airport's efforts to have gates available to nonincumbents a factor in FAA's decisions on federal grants to airports. The Department did not concur with that recommendation, stating that the gate access issue would be better addressed on a case by case basis. We noted that incumbent airlines may be in a position to use their contractual arrangements with local airport authorities to block new entry by influencing access to airport infrastructure and services. Such behavior may ,under certain circumstances, give rise to an unfair or deceptive practice or an unfair

method of competition, or may even be a violation of the Sherman Act. The Department said it will investigate allegations that carriers are unfairly blocking competition through such practices and called for carriers to come forward if they believe they are being unfairly denied access.

Let me also mention three other issues that I know are of concern to Members of this Committee. First is the perimeter rule at Washington National Airport. This rule was created by Congress in its oversight capacity over Washington's two airports. While the Department has been presented arguments for and against modification of the perimeter rule, we take no position on whether it should be modified. We recognize that this is an issue, like other issues of this kind, that Congress must decide.

Second, we are sensitive at the Department to the special needs of small communities. In January I traveled to Montana and North Dakota to hear directly from people in those rural states their suggestions for improving their access to the national transportation system. Those meetings were very helpful.

Third, the new funding source for the Essential Air Service program will provide an adequate subsidy level to maintain and improve essential service for our smallest communities beginning October 1, 1997. We have already begun taking necessary steps to implement higher levels of service at that time. We have also made effective use of our slot exemption powers to provide greater small community access to Chicago's O'Hare Airport.

Mr. Chairman, the Department is committed to completing a thorough examination of all of the issues I have discussed today. We will continue to work with the Justice Department and to develop DOT policies that help to ensure that the benefits of competition are available to air travelers in all sections of the country. At the same time we want to be careful not to impose policies or standards that would impair the benefits of the competitive process.